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D/E Statement on ORR Contribution to NIE 100-5-54, 6 December 1954

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1. D/E finds itself in agreement with those parts of the paper which relate to the effects of export controls and which are sufficiently specific to have substantive meaning, for example, the excellent specific analysis of the effects of export controls on pages 9 - 11.

2. D/E considers the material relating to "the long run" as largely irrelevant to the present problem. Those who have had principal responsibility for the export control program, while not unmindful of long run consequences, have always considered the program aimed primarily at short run objectives. The example of the imposition of a tariff on Swiss watches and of how the consequent effects work themselves out in the long run provides scant analogy to a flexible and selective system of strategic trade controls which are almost continuously subjected to change and adaptation to dynamic situations.

Fundamentally, in China, we are dealing with a touch and go situation. If Red China were to achieve a short term economic-military buildup, it might lose perspective and be tempted, like Hitler, to attack and thus start World War III. To speak of "long run" under these conditions is inappropriate. These circumstances render it imperative that the effects of western strategic controls be analyzed accurately and in specifics with as much supporting statistics and other facts as possible. This short term national security approach is conspicuously lacking in the analysis.

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3. It is realized that too little time was allowed for the preparation of the subject paper. Also it has been pointed out that the terms of reference were not ideally oriented to the original request for the NIE. For example, the terms of reference call for consideration of US unilateral action which is actually out of the context of the COCOM-CHINCOM mechanism under study. The final multilateral position is bound to be a determinant of US unilateral action. It is therefore premature to examine at this time what US unilateral action against China might be taken until the outcome of COCOM-CHINCOM negotiations is available. The inclusion of the idea of unilateral US action (abolition of US import and financial controls) has resulted in confusion in the analysis.

4. It should be borne in mind that the request for the NIE originated in FEEDWG. The hope was for an NSC directive relative to CHINCOM controls with special reference to levels for evaluating commodities. Ultimately the details of controls along lines indicated by NSC would be developed in an interagency group and would then be conveyed to the US negotiators in COCOM/CHINCOM. Both the agencies and the negotiators need more precise control guidance than is offered in the current paper.

5. In discussing various courses of action, the paper fails to differentiate between the general effects and the effects upon war potential; nor does it differentiate clearly between past and future, between imports for consumption and imports for industrialization, or between imports of military equipment and total imports. It speaks of transshipments through Gdynia without any qualitative appraisal of the significance of this tonnage.

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The matter of smuggling (tin-plate, ball bearings, tires, kerosene, wire-rope, ship plate, tool bits) is almost not dealt with at all.

6. It would appear that the paper should give consideration to the possibilities inherent in various control levels. The maximum position would be one in which the present level is actually raised, as indicated in the section on criteria. The maintenance of the present level of controls would envisage no change from the present. However, a realistic relaxation would result from only embargo of old and new IL I, II and III or this embargo plus selected items from the China Special List. A still lower control level would be only embargo on IL I, and of quantitative control on IL II and surveillance on IL III (the present level of control to USSR and European satellites). A final possibility might be that of decontrol of all but IL I items with embargo on these only. Only two of these possible control levels have been partially treated in the ORR paper.

The requirements of FEEDWG and CHINCOM would suggest that each of the above control levels should be examined on a commodity basis, by categories at least, against appropriate criteria. There would then be more concrete guidelines to indicate the point below which it would be considered inadvisable for the US negotiators to go in the relaxation of controls.

7. D/E finds unconvincing the statements in this and other papers that the Soviet bloc has provided Communist China with all essential requirements for rapid industrial growth and military buildup. The contribution of bloc capital goods to the increase in industrial output from 1950 to 1954 should be stated in perspective. The increases through at least 1952 represent general restoration toward production levels before

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the disruptions of the Chinese civil war and thus do not constitute "growth" in the sense of secular trend. The recovery was due in large part to intensive utilization of industrial machinery and equipment taken over from the Japanese and the Nationalists, the latter largely of U.S. origin, probably exceeding in quantity the industrial equipment imported from the Soviet bloc. It would be more accurate to state (in lieu of first sentence, page 3, ORR contribution) that with the aid of some new capital equipment imported from the European Soviet bloc, Communist China has made noteworthy progress in restoring and expanding its industrial production generally to levels higher than those attained by the Nationalists or the Japanese.

8. The statement that industrial production has increased at the rate of 28 percent annually from 1950 through 1953 is misleading. An average of three year to year increases as dissimilar as those hereunder consideration (23%, 1950-51; 45%, 1951-52; 17%, 1952-53) does not give a meaningful rate of change. An explanation is necessary that 1950 represented a very low level consequent on civil war (or revolution); similarly recovery from that level to some pre-revolution level would require some precise description to be significant. Moreover, the reader might well be cautioned against attributing even a major part of the "large" 28 percent annual increase to the honeymoon association of Communist China with the Soviet Union while forgetting the UNRRA and ECA aid programs of 1945-48 and the contributions of former Japanese properties.

9. The presentation of the potential foreign exchange increment from relaxed controls is considered inadequate. The bilateral analysis should be extended to include other countries and to cover the triangular trade

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potential, sources of "remittances" other than the U.S., the extent of blocked foreign assets, and the effect on Communist Chinese exports of a possible large expansion in the next few years of national incomes in Western <sup>countries</sup> ~~incomes~~ and Japan.

10. The ORR paper is mainly historical -- a backward look, and consequently does not provide the carefully calculated forecast of future consequences and developments which are needed for policy guidance.

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